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Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C.

In re	)	
	)	
Review of the Prime Time Access Rule, Section 73.658(k) of the Commission's Rules	)	MM Docket No. 94-123
	)	DOCKET FILE COPY ORIGINAL

Comments of the Staff of the Bureau of Economics of the Federal Trade Commission*

March 7, 1995

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* This comment represents the views of the staff of the Bureau of Economics of the Federal Trade Commission. They are not necessarily the views of the Commission or any individual Commissioner. Inquiries regarding this comment should be directed to Michael Vita (202-326-3493) of the FTC's Bureau of Economics.

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I. Introduction

The staff of the Bureau of Economics of the Federal Trade Commission is pleased to respond to this Notice of Proposed Rulemaking ("NPRM") through which the Federal Communications Commission (FCC) seeks comments on proposals to relax or eliminate the Prime Time Access Rule ("PTAR").[2] The PTAR was adopted in 1970, in conjunction with the Financial Interest and Syndication ("Fin-Syn") rules.[3] The PTAR basically prohibits network-affiliated television stations in the top 50 television markets from broadcasting more

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[2] 47 C.F.R. § 73.658(k).

[3] The Fin-Syn rules limited broadcast networks' ability to integrate vertically into the sale and distribution of syndicated programming. The Fin-Syn rules are scheduled for expiration in November 1995.

than three hours of network or "off-network" (i.e., rerun) programs during the four prime time viewing hours. This comment provides observations about possible economic costs and benefits from relaxing or eliminating the rule and presents both current and historical data that may help the FCC assess the rule's present and past competitive consequences. This comment concludes that, when assessed under a "public interest" standard which seeks to promote consumer welfare, justification for continuing this rule is questionable.

II. Expertise of the Staff of the Federal Trade Commission

The FTC is an independent regulatory agency responsible for preventing unfair methods of competition and unfair or deceptive acts or practices.[4] In response to requests by federal, state, and local government bodies, the staff of the FTC often analyzes regulatory or legislative proposals that may affect competition or the efficiency of the economy. In the course of this work, as well as in antitrust and consumer protection research, nonpublic investigations, and litigation, the staff applies established principles and recent developments in economics to the analysis of competition and consumer protection matters.

The staff of the FTC has commented on a number of issues involving the FCC and its responsibilities, beginning with a 1924 report to the House of Representatives about competition issues in radio.[5] More recently the staff has submitted comments to the FCC on

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[4] 15 U.S.C. §§ 41-49.

[5] Federal Trade Commission, Report on the Radio Industry, GPO, 1924.

television and radio ownership rules and policies;[6] competition, rate deregulation, and cable television service;[7] common ownership of cable systems and national television networks;[8] the "must carry" rules applied to cable television systems;[9] the rules requiring licenses to be held for three years before being transferred;[10] network ownership of financial interests and syndication rights;[11] spectrum allocation and standards for digital audio broadcasting,[12] and the regulation of "900" telephone number services.[13]

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[6] Reply Comments of the Staff of the Bureau of Economics of the Federal Trade Commission, In re Revision of Radio Rules and Policies, MM Docket No. 91-140, September 5, 1991; Comments of the Staff of the Bureau of Economics of the Federal Trade Commission, In the Matter of the Commission's Regulations Governing Television Broadcasting, MM Docket No. 91-221, September 24, 1992.

[7] MM No. 89-600 (1990).

[8] CT No. 82-434 (1982).

[9] MM No. 90-4 (1991).

[10] BC No. 81-897 (1982).

[11] MM Nos. 82-345 (1983) and 90-162 (1990).

[12] GEN No. 90-357 (1991).

[13] CC No. 91-65 (1991).

III. The Prime Time Access Rule

The PTAR states that commercial television stations owned by or affiliated with a national television network[14] in the 50 largest television markets[15] may not devote more than three hours of "prime time"[16] to the presentation of network or off-network (i.e., rerun) programming.[17] The PTAR was adopted in 1970 (in conjunction with the Financial Interest and Syndication Rule) to mitigate several perceived problems in the supply of television programming. According to the NPRM (¶ 1), "PTAR was promulgated in 1970 in response to the concern that the three major television networks — ABC, CBS, and NBC — dominated the program production market, controlled much of the video fare presented to the public, and inhibited the development of competing program sources. The Commission believed that PTAR would increase the level of competition in the independent production of programs, reduce the networks' control over their affiliates' programming decisions, and increase the diversity of programs available to the public. "

The NPRM identifies three basic ways the PTAR may have affected competition in relevant markets. First, by designating a portion of prime time for nonnetwork programming, independent producers would find it easier to sell programming to network affiliates in large

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[14] For the purpose of the PTAR, a "television network" is an entity that provides more than 15 hours of prime time programming per week on a regular basis to at least 75 percent of television households nationwide (NPRM, ¶ 9). By this definition, there are currently three networks subject to the rule (ABC, CBS, and NBC).

[15] The 50 largest television markets accounted for about 75 percent of total television households in the United States at the time the PTAR was adopted.

[16] For purposes of the rule, "prime time" is the 7-11 p.m. time slot in the Eastern and Pacific time zones, and the 6-10 p.m. time slot in the Central and Mountain time zones.

[17] There are several exceptions to this restriction; see 47 C.F.R. § 73.658(k)(1)-(6).

markets, which in turn would strengthen existing producers and encourage the entry of new ones. This financial strengthening of independent producers would result, in part, from higher program prices for independently produced programming that ostensibly would result from a reduction in the supply of network and off-network programming to network affiliates (NPRM, ¶ 31).

Second, the FCC intended that the rule reduce network dominance and increase the affiliates' autonomy in choosing programming by preventing major-market affiliates from showing network-supplied programming during a segment of prime time. According to the NPRM (¶ 40), "the rule was intended to increase the chances that the programming appearing on an affiliated station would reflect true viewer preferences."

Third, the PTAR came to be regarded (NPRM, ¶ 45) as a mechanism for "providing independent stations with a competitive advantage over competing network affiliates" by placing an explicit constraint on the ability of network affiliates to televise popular programming during the access time period. According to the NPRM (¶ 45), "since the Top 50 Market Affiliates [would] have a more limited range of choices in placing programming on their stations, the independent stations receive two competitive advantages: (a) less competition for viewers, and (b) less expensive programming."[18]

The FCC now wishes to "undertake a rigorous economic and policy analysis in this proceeding to assess the extent to which the rule serves the Commission's 'public interest'

[18] The NPRM states (¶ 45) that "[t]he rationale for giving these advantages has been explained as a correction for inherent competitive disadvantages shouldered by independent stations, such as the technological impediments they face by virtue of the fact that most of them have been relegated to the UHF band."

mandate to maximize consumer welfare, as opposed to merely protecting individual competitors in the communications industry."[19] In particular, the FCC "seeks to evaluate the factual and economic assumptions underlying [the] PTAR to ascertain whether the rule operates to achieve its intended effects, and [to determine] what unintended effects it may also cause." The information gathered by the FCC in this inquiry will be used in the FCC's "ultimate cost/benefit calculation" as to whether the PTAR will be revised, retained, or eliminated. The FCC is also concerned about whether the PTAR achieves non-competition based public interest goals (NPRM, ¶ 3). This comment is limited to discussion and analysis of competitive effects.

Some of the competitive issues that the FCC is examining may usefully be addressed by principles applied in antitrust analysis. In carrying out its antitrust enforcement responsibilities under the Clayton Act,[20] the Sherman Act,[21] and the Federal Trade Commission Act,[22] the FTC focuses on conduct that would create or enhance market power, defined as the ability to profitably maintain prices above competitive levels for a significant time period.[23] Consistent with the goals articulated in the NPRM, the antitrust laws are

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[19] NPRM, ¶ 32.

[20] 15 U.S.C. § 18 (1988).

[21] 15 U.S.C. § 1 (1988).

[22] 15 U.S.C. § 45 (1988).

[23] The exercise of market power may take place along dimensions other than price, such as product quality, service, or innovation. Market power can also be exercised by purchasers of a good or service (monopsony power).

concerned with "the protection of competition, not competitors."[24] Accordingly, we believe the analytical approach used in antitrust enforcement may prove useful as a means for analyzing the consumer welfare implications of the PTAR.

IV. Economic Relationships Among Program Producers, Networks, and Stations

To facilitate our analysis of the issues raised in the NPRM, we use the following framework. First, we assume (as is standard in antitrust analysis) that firms in the relevant markets affected by the rule seek maximum profits. Second, we assume that the principal economic function of a commercial broadcast television station is to attract an audience with its programming and to sell access to that audience to advertisers. A profit-maximizing broadcast television station will attempt to assemble an array of programming attractive to an audience that advertisers value. The audience's value will likely be determined not only by its size, but by its other characteristics (such as income, age, or gender).[25] A broadcast television station competes with other geographically proximate television broadcasters for access to the audience that can receive the broadcaster's telecast.

Networks of local broadcast stations take advantage of substantial scale economies and lower transactions costs in programming acquisition and distribution and in advertising sales. The essential function of a network is to be an intermediary between advertisers and program producers on one hand, and local stations on the other.

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[24] Brown Shoe Co. v. United States, 370 U.S. 294, 320 (1962).

[25] Owen and Wildman, Video Economics (Cambridge: Harvard University Press, 1992), p. 3.

Three propositions follow from these economic relationships among program producers, networks, and local affiliates. The first is that a profit-maximizing network does not necessarily have an incentive to engage in the production of television programming. As a profit-maximizing entity, a network will try to acquire programming for distribution to its affiliates at minimum cost — any other choice involves a sacrifice of profits. Whether a network chooses to produce programming internally, or instead acquire it from independent program producers, will depend upon a variety factors, including the technological characteristics of program production, the costs of market transactions, and the competitiveness of the market for new program supply.[26] Absent economies from vertical integration, or considerations of market power (which do not appear to be a problem here[27]), a profit-maximizing network will try to procure its programming from independent producers who compete vigorously with one another for the network's patronage.[28]

The second proposition is that networks and their affiliated stations each have an interest in televising an array of programming that maximizes the profits from the sale of

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[26] See, e.g., Coase, "The Nature of the Firm," Economica, n.s., 4 (1937), 386-405.

[27] See note 33, infra.

[28] Similarly, a television network will not necessarily try to acquire the syndication rights to programming that it acquires from independent program producers for first-run network exhibition. Prior to the adoption of the Fin-Syn rule, the networks collectively accounted for 18.5 percent of syndicated program sales by hours. Pre-1970 data suggest that the networks did not always purchase syndication rights for programs exhibited on their network. Alfred Kahn ("Comments on the Federal Communications Commission's Financial Interest and Syndication Rules," January 25, 1983) examined the extent to which CBS acquired the syndication rights to new "prime time" series from 1963 to 1971. Overall, CBS purchased these rights to domestic syndication 36 percent (25 out of 69 instances) of the time. See also Crandall, "The Effect of Television-Network Program 'Ownership'," Journal of Law and Economics 14 (1971), 385-412, p. 398.

advertising.[29] When a network takes an action that increases the value of an audience (for example, when it acquires broadcast rights to a popular program), this increases the amount that the network can charge an advertiser for access to that audience, which in turn increases the amount that the network would willingly pay an affiliate to televise (i.e., "clear") that program. It also increases the amount that the affiliate can charge advertisers for direct sales of advertising time.[30] A network and its affiliates will, of course, bargain over the division of any increase in profits that results from such an action — each will seek to leave the other with an amount just sufficient to cover opportunity costs — but in principle both can be made better off by any programming choice that increases total advertising profits.[31]

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[29] For a detailed analysis of the network-affiliate relationship, see, e.g., Besen and Soligo, "The Economics of the Network-Affiliate Relationship in the Television Broadcasting Industry," American Economic Review 63 (1973), 259-68; and chapter 5 ("Economic Analysis of the Relationship Between Networks and Their Affiliates") in Besen, Krattenmaker, Metzger, and Woodbury, Misregulating Television (Network Dominance and the FCC). Chicago: University of Chicago Press, 1984. The NPRM (¶ 35) also notes how profit incentives could play a determinative role in program selection.

[30] The typical network-affiliate contract reserves for the affiliate a certain amount of prime time advertising time (known as "adjacencies") that the affiliate can sell directly to advertisers.

[31] That networks and their affiliates have an incentive to maximize joint profits should not be taken to mean that all network programs will be carried by every affiliate. There will be instances where it is more profitable for an affiliate to carry a nonnetwork program (e.g., a locally broadcast baseball game) than it is to carry the network program. To determine whether it is profitable to clear a network program, the affiliate will compare its net revenues from carrying a nonnetwork program (i.e., local advertising revenues minus production costs) to the revenues it receives from carrying the network program (i.e., direct payment from the network, plus revenues from sales of "adjacencies" (see note 30, supra)). If the former amount exceeds the latter, the network program will be preempted by the local program.

To see that, in principle, it is in the mutual interest of both the network and the affiliate for this pre-emption to occur, consider the following example (adapted from Besen et al., supra note 29, pp. 53-57). To simplify, assume that the affiliate receives no "adjacencies", but is compensated for network program clearance solely by direct network payments. Suppose that if a particular affiliate clears the program in question, the network receives an additional $55 in revenues from the national advertisers to whom it is selling time. This $55

The third proposition rests on the principle that economic entities normally will have a profit incentive to reduce or limit competition from other entities operating at the same stage of production (i.e., horizontally-related entities), but increase the degree of competition in vertical (or complementary) stages of production. Other things equal, a network will try to minimize the extent to which it competes with other networks, but would prefer to prevent the creation or exercise of market power in upstream (i.e., programming) as well as downstream (i.e., local broadcasting) markets. Similarly, other things equal, a local broadcaster would profit if it could reduce competition from other local broadcasters (and any other competitors for the sale of advertising), but would prefer competition at the network or programming levels.

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is the maximum amount that the network would pay that affiliate to clear the program. Suppose that as an alternative, the affiliate could televise a local baseball game, yielding the affiliate revenues (net of production costs) of $60.

In theory, both the network and the affiliate can earn higher profits if the baseball game preempts the network program. Consider first a situation where the network can force the affiliate to clear the program without compensation (thus allowing the network to keep all $55 in incremental revenue). If instead the game is televised, the affiliate could offer the network $56 (making the network better off by $1) and keep $4 for itself (thus increasing its profits by $4). Alternatively, suppose the network is paying the affiliate the full $55 to clear the program (i.e., the network earns no incremental profits from this affiliate's clearance). If the game is shown instead, the affiliate could offer the network $1 (thus increasing the network's net profit by $1) and increase its own profits by $4 (= $60 - $55 (foregone network compensation) - $1).

It was never the case, even before PTAR, that affiliates cleared all network programming. In the 1950s, the prime time clearance rate was between 80 and 90 percent; by the 1970s the rate had risen to about 95 percent (See FCC Network Inquiry Special Staff Report, New Television Networks: Entry, Jurisdiction, Ownership, and Regulation (vol. II) October 1980, ("Special Staff Report"), pp. 262-63). Recently the clearance rates have fallen to about 90 percent. See Lin, "Changing Network-Affiliate Relations Amidst a Competitive Video Marketplace," Journal of Media Economics 7 (1994), 1-12, p. 3.

V. Issues Raised in the Analysis of the PTAR

A. Increasing Opportunities For Independent Producers

The NPRM notes (¶ 33) that a principal motive for adopting the PTAR was to increase opportunities for independent producers of television programs to sell programming to top 50 Market network affiliates for prime time broadcast. According to the NPRM (¶ 34), "the carving out of a time slot for independently produced programs would appear to increase the demand for them, thus raising prices and encouraging entry of new firms producing such programs." The NPRM (¶ 33) requests analysis and empirical evidence that would shed light on whether the PTAR has increased the net number of independent producers of television programs or the net quantity of independently produced programming, or has decreased the net value of programming produced for prime time network telecast. Given the proliferation of outlets for nonnetwork programming, it is likely that the PTAR is no longer critical to the concerns expressed by the FCC in the NPRM.

It is not clear that the PTAR has affected the number of independent production entities. This point is relevant for assessing the argument put forth by PTAR proponents that "once the protection of PTAR is lifted, an entire segment of program supply could wither, leaving, over the long run, a significant reduction of total program suppliers [emphasis added]" (NPRM, ¶ 34). The economic viability of independent production entities would face such risks only if networks chose to supply a greater portion of their programming demands with in-house production. Because networks have an incentive to arrange for an efficient supply of programming, networks would have an incentive to integrate vertically into program production only if (1) in-house production is more efficient than external supply;[32] (2) independent program producers are exercising market power (which implies that vertical integration allows networks to obtain competitively-priced programming); or (3) the networks could, through vertical integration, acquire horizontal market power in the market for television programming.[33] From a competition policy perspective, vertical integration by the networks into program production would raise concerns only under the third rationale.

Empirically, it is difficult to support the proposition that the economic viability of independent program production entities would be threatened were PTAR to be removed. Indeed, at the time of PTAR's adoption, the quantity of network prime time programming

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[32] As we noted in our comments on the Fin-Syn rule (supra note 11), integration by the networks into program production may be a means for achieving economic efficiency. In particular, the comments noted that vertical integration may represent the least-cost method of forestalling opportunism by program suppliers. If high contracting costs or the existence of uncertainty make it difficult to prevent opportunism contractually, joint ownership of the specific assets (i.e., backward integration by the networks) may be the least costly (and perhaps the only) means for preventing opportunism. The Fin-Syn rules, by preventing the networks from taking any ownership position in the syndication rights of a program, prevented the use of joint ownership as solution to this problem. If joint ownership or vertical integration is the most efficient method for reducing the networks' exposure to these risks, the attenuation of the networks' ability to integrate vertically may increase their risk exposure, and thereby ultimately reduce welfare.

[33] It is conceivable that a monopoly network, or a cartel of colluding networks, might seek to monopolize the supply of new programming (e.g., by entering into contracts with program suppliers that prevent the latter from producing programs for, or syndicating programs to, other distributors or exhibitors), thus preventing entry by new networks. There is no empirical evidence that the networks actually pursued such a strategy, however. Indeed, as noted earlier (supra note 28), in most instances networks chose not to acquire the syndication rights to network programming. The allegation that networks might attempt to anticompetitively "warehouse" (i.e., purchase the syndication rights to the programming and then refuse to license the programming to independent stations) off-network programming was analyzed in greater detail in our 1983 and 1990 comments on the Financial Interest and Syndication Rules. See note 11, supra. In those comments, we concluded that available empirical evidence did not support the "warehousing" hypothesis.

acquired from independent production companies had increased substantially over the course of the preceding decade. During that period, programming acquired from independent production sources increased from about 71 percent to about 84 percent of all prime time network programming (see Table 1); for entertainment programming, the percentages are 79 and 96, respectively (see Table 2). Today the three networks acquire about 57 percent of their prime time programming from external sources (see Table 3).

Tables 3 through 5 present data on the market shares of producers of prime time network programming. These data suggest that there are (and were at the time of PTAR's adoption), many independent suppliers of programming for both network and nonnetwork broadcast; that the minimum efficient scale of production is low; and that there are no obvious impediments to entry and growth by new suppliers of programming.[34]

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[34] As the Network Inquiry Special Staff noted when comparing 1970 and 1977 market share, Warner was not ranked in the top twenty in 1970, but rose to number two in 1977; MTM and Lorimar did not exist in 1970, but were ranked fourth and fifth, respectively, in 1977. See Special Staff Report, supra note 31, p. 560. Comparing 1994 to 1977 shows similar instability in the identity, and relative positions, of the top twenty producers. The Kendall rank correlations (which show the correlation between the market share rankings in different time periods) are low; statistically, one cannot reject the hypothesis that they are equal to zero. The correlation coefficient between the 1970 and 1977 rank is .086; for 1977 and 1994, it is .062; for 1970 and 1994 it is .094.

Table 1

Total Network Evening Programming, by Production Source		
	1957	1968
(1) Network produced	28.7	16.3
(2) Independently produced (licensed to advertisers)	32.8	3.3
(3) Independently produced (licensed to networks)	38.5	80.4
Total independent production [(2) + (3)]	71.3	83.7

Source: PTAR, First Report & Order, pp. 389-90.

Table 2

Network Evening Entertainment Programming, by Production Source		
	1957	1968
(1) Network produced	21.2	4.1
(2) Independently produced (licensed to advertisers)	35.6	3.8
(3) Independently produced (licensed to networks)	43.2	92.1
Total independent production [(2) + (3)]	78.8	95.9

Source: PTAR, First Report & Order, pp. 389-90.

Table 3

LEADING NETWORK SUPPLIERS: PRIME TIME, FALL 1994	
SUPPLIER	SHARE OF PROGRAMMING HOURS (%)
ABC Productions & ABC Sports	17.59
Warner Brothers	14.81
CBS Network Productions	13.89
NBC Television Network	11.11
Universal	11.11
Disney	5.56
20th Century Fox	4.63
Columbia Tristar	3.70
Alliance	1.85
Carsey Werner	1.85
Cosgrove Meurer	1.85
Paramount	1.85
Stephen Bochco Productions	1.85
Silverman Co./Viacom	1.85
Witt Thomas	1.85
Castle Rock	.93
Mozark	.93
Shukovsky English Entertainment	.93
Spelling	.93
Wind Dancer	.93

Source: Daily Variety, August 30, 1994.

HHI = 1063

Table 4

Twenty Leading Network Suppliers: Prime Time, 1977	
Supplier	**Share of Programming Hours (%)**
Universal	18.4
Warner	6.7
Spelling Goldberg	6.1
Lorimar	5.4
MTM	5.3
Columbia	3.6
MGM	3.5
Paramount	3.5
Aaron Spelling	3.2
Twentieth-Century Fox	3.2
Walt Disney	2.9
Tandem	2.9
Quinn-Martin	2.7
Tat	2.4
Toy	2.2
CBS	2.0
Four D	2.0
Whacko	1.7
Schick-Sunn Classics	1.6
David Gerber	1.6

HHI = 617[a]

[a] The data in the table account for 81 percent of total prime time programming hours. Because data on the remaining share were not available, the HHI calculation assumes that the remaining 19 percent is divided equally among 13 producers, each with a 1.5 percent share. This calculation places an upper bound on the value of the HHI. Source: Special Staff Report, supra note 31, p. 573.

Table 5

Twenty Leading Network Suppliers: Prime Time, 1970	
Supplier	Share of Programming Hours (%)
Universal	12.8
Twentieth-Century Fox	7.3
Paramount	6.4
Columbia	6.1
MGM	4.5
Filmways	3.6
ITC	3.0
Harbour	2.6
Spelling/Thomas	2.3
Talent	2.2
Teleklew.	2.0
CBS	1.9
Walt Disney	1.9
Leonard Freeman	1.8
NBC	1.8
Sullivan	1.8
Peekskill	1.7
Xandu	1.7
Van Bernard	1.5
Glenco	1.5

HHI = 430[b]

[b] The data in the table account for 68 percent of total prime time programming hours. Because data on the remaining share were not available, the HHI calculation assumes that the remaining 32 percent is divided equally among 23 producers, each with a 1.4 percent share. This calculation places an upper bound on the value of the HHI. Source: Special Staff Report, supra note 31, p. 572.

B. Reducing the Ability of Networks to Dictate Programming Choices

In the decade preceding adoption of the PTAR, the identity of program licensees changed dramatically. Overall, the quantity of independently-produced programming licensed to nonnetwork entities (e.g., advertisers) fell considerably (see line (2) in Tables 1 and 2), while the amount licensed directly to networks increased by a large amount.[35] This change — and the resulting "dominance" of the three major networks as programming licensees — provided much of the impetus for the adoption of PTAR in 1970. According to the First Report & Order,"

> network affiliates in 1968 carried an average of between 3.3 and 4.7 . . . hours a week of nonnetwork programming between the hours of 7 to 11 p.m. out of the total of 28 hours. And, as we shall show, nonnetwork programming is increasingly composed of off-network programs. A concomitant to this control of access has been the virtual disappearance of high cost, prime time syndicated programming, the type of programming (other than feature motion pictures) which must be most relied upon as competition for network-supplied entertainment programs."[36]

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[35] The Special Staff Report (supra note 31, pp. 334-38), analyzed the reasons for the decline in advertiser-produced or -licensed prime time programming. The Special Staff argued that, given the high mortality rate for new series, it became more economical for advertisers to buy spots on numerous programs, rather than buying most of the spots on a smaller number of programs. The Special Staff also argued that an advertiser could obtain access to a more diverse audience by purchasing spots on a variety of different programs. This latter incentive would be particularly important for multiproduct advertisers, who might wish to target different products to different audiences.

[36] 23 F.C.C. 2d 382, 385.

The FCC intended that PTAR would permit affiliates to select programming from a wider range of sources than the three networks, providing affiliates an opportunity to better cater to viewers' tastes. As stated by the NPRM (¶ 40), "the rule was intended to increase the chances that the programming appearing on an affiliated station would reflect true viewer preferences. The view was that while the network would dictate one program for the access period, the rule would permit the affiliate to choose from a range of choices."

Much of the analysis of the PTAR has questioned the accuracy of this view.[37] Because both networks and affiliates earn their profits by selling audience access to advertisers, both have a mutual interest in televising programming that will be attractive to audiences (hence advertisers). Neither the network nor the affiliate has an incentive to air programming that would prove unattractive to audiences, since advertisers would pay little for the opportunity to advertise on this programming.[38]

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[37] See, e.g., Crandall, supra note 28; Special Staff Report, supra note 31, p. 533; Besen et al., supra note 29, chapter 5. A related argument (i.e., that networks' ownership interests in network programming would distort networks' programming choices, to the detriment of independent producers and viewers) was employed to justify the Financial Interest and Syndication Rules (see 23 F.C.C. 2d 382, 392-99 (1970)). Crandall's econometric analysis of the networks' program retention decisions in the period preceding adoption of the PTAR and Fin-Syn rules found few statistically significant relationships between networks' ownership of syndication rights (or profit shares) and the probability that a program would be retained in the prime time lineup from one year to the next. Where significant relationships were found, the sign of the relationship was the opposite of that predicted by the favoritism hypothesis (i.e., the study found that programs were more likely to be dropped when the network owned the distribution rights). See Crandall, supra note 28, pp. 400-406.

[38] Thus, as noted above, while a network and its affiliates will likely engage in hard bargaining over the division of any economic rents, they have a mutual incentive to seek to maximize the total amount of rents to be divided. From the perspective of economic efficiency (and assuming the absence of transactions costs and information disparities that might impair achievement of the efficient outcome), the concern expressed in the NPRM (e.g., ¶¶ 43-44) about the relative bargaining positions of networks and their affiliates seems somewhat

Requiring network affiliates to air nonnetwork programming probably has not changed programming much, as long as the number of programming outlets in a geographic market remained unchanged.[39] As observed in one early analysis of the rule, "[s]tation managers will be subject to the same market forces which faced network executives, who merely provided brokerage for them. As long as there are no more than three stations in most markets, the most profitable programming will continue to be similar to that provided by three networks [emphasis original]."[40] Given the number of stations in an individual local television market, each station will consider a number of factors when choosing which program to show in a particular time slot: (1) the size and demographic characteristics of the audience that would

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misplaced. The relative bargaining positions of a network and its affiliates may well have shifted over time, with a consequent change in the distribution of economic rents between the parties. What has not changed is the mutual incentive of a network and its affiliates to air programming that is attractive to audiences, and therefore valuable to advertisers.

[39] In § V.C, we discuss whether PTAR would have likely contributed to the growth in the number of outlets (i.e., new broadcast stations) for independently-supplied programs.

[40] See Crandall, supra note 28, p. 407. Other analysts reached the same conclusion. See FCC Network Inquiry Special Staff Report, supra note 31, p. 533; Besen et al., supra note 29, pp. 55-59, 172 ("[t]he rule was said to avoid subjecting viewers to a limited choice of programs, all of which had been found acceptable to one of only three firms. By substituting three affiliates for three networks, the rule does nothing to alleviate this 'funnel' effect."). This view differs from that presented in the First Report & Order (23 F.C.C. 2d 382, 387), which stated that "[f]ormerly, when many program producers dealt directly with sponsors, their market for network television programming was composed of 50-100 potential buyers. Now, that market has dwindled for all practical purposes to three." We agree with the view that the binding constraint on a programmers' access to audiences is the number of television channels in local markets. Regardless of the number of potential advertiser licensees for independent programming, those advertisers must still bid among themselves for access to the air time on this limited number of channels. If local stations attempt to maximize profits, this air time will be sold to those advertisers who are willing to pay the most for it. But the amount that an advertiser would pay for the right to televise its own program will be determined by the same factors that determine the amount it would pay for advertising time on a network-supplied program. Because the same economic incentives are present under both advertiser-licensing and network-licensing of programs, both likely would lead to similar programming mixes.

view each programming alternative; (2) the amount that advertisers would willingly pay for access to those audiences; (3) the degree of competition faced by the station; and (4) the costs of acquiring programming. Neither (1), (2), nor (3) is affected directly by the PTAR.[41] Any effect on item (4) (programming costs) would be unlikely to serve viewers' interests (see § V.C, below).

We recognize that the networks and their affiliates may not invariably air programming that maximizes their joint profits.[42] As noted earlier (supra note 38), networks and their affiliates will bargain hard over the distribution of profits, and it is conceivable that each party will take actions to improve its negotiating position that will sometimes result in a failure to maximize joint profits. Additionally, the presence of high transactions costs sometimes might also impede joint profit maximization. A mutual incentive exists for networks and their affiliates to eliminate these impediments, however, either through contract or through ownership integration.[43]

The NPRM (¶ 42) expresses doubt whether the PTAR is necessary to serve its intended purposes. Since 1970 the networks' position has changed, making it unlikely that they "would attempt to force their affiliates to take unpopular programs or programs necessarily different from those the affiliates themselves would choose" (NPRM, ¶ 42). The principal reason given

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[41] Section V.D, below, discusses the possible indirect effects PTAR may have had on competition among local broadcasters.

[42] For a discussion of this issue, see Besen et al., supra note 29, pp. 59-64; Owen and Wildman, supra note 25, pp. 171-72.

[43] Besen et al. note, however, that restrictions on networks' ownership of stations, and on the form of network-affiliate contracts, may impair the ability of networks and their affiliates to avail themselves of these mechanisms.

is that affiliates now have more affiliation options, hence greater bargaining power.[44] Other things equal, the presence of the Fox network will induce the other three networks to offer their affiliates more attractive financial incentives, as the latter now have a competitive alternative — affiliation with Fox — that they lacked previously. Indirect evidence, in the form of changes in affiliation, suggests that the presence of Fox has significantly perturbed the equilibrium relationships that had previously prevailed between the three major networks and their affiliates. According to Broadcasting & Cable,[45] CBS lost its affiliates (to Fox) in Dallas, Cleveland, Phoenix, Detroit, Atlanta, Milwaukee, and Austin. NBC lost its affiliate (to ABC) in Baltimore, and to Fox in Kansas City. ABC lost affiliates to Fox in Greensboro and Birmingham. Thus, even though we would question on an analytical level the proposition that profit-maximizing networks would dictate that their affiliates carry unpopular programs, we share the NPRM's view that increased competition among networks would make coercion less

[44] Not all of the changed circumstances identified in the NPRM would imply that such "coercion" would be less likely. Affiliates now have more choices, but so do networks. In 1970, there were 677 commercial broadcast television stations, while in 1993, there were 1137, an increase of about 68 percent (1994 Television & Cable Factbook, p. I-7). The availability of additional potential outlets for its programming gives each network, other things equal, an increased ability to negotiate favorable affiliation terms. Empirical information on compensation paid to network affiliates suggests that this compensation is lower, other things equal, when there are competing independent stations in the same local market. The FCC Network Inquiry Special Staff estimated the statistical relationship between the compensation paid to affiliates for clearing network programming and a variety of explanatory variables, including whether the affiliate faced competition from independent stations. In virtually all versions of this equation, the presence of independent stations exercised a negative and statistically significant impact on compensation. Of course, though the level of compensation paid might vary across markets, an affiliate must always receive sufficient revenue to cover its opportunity cost of production. See Special Staff Report, supra note 31, pp. 269-86. Also see Besen, "The Value of Television Time," Southern Economic Journal 42 (1976), 435-41.

[45] "Affiliates Change Partners Again," June 27, 1994, p. 6.

likely to succeed.[46]

Last, we note this rationale for the PTAR — freeing network affiliates to choose programs that better reflect true viewer preferences — appears somewhat inconsistent with the third rationale now offered for the rule — providing local independent broadcast stations with a competitive advantage over network affiliates. PTAR was intended in part to ensure that local network affiliates could choose programs that better reflected their viewers' preferences, a result that should have made them more popular and competitively successful. That scenario is somewhat inconsistent with the third rationale offered for PTAR, that it tends to afford competitive advantages to independent stations by handicapping network affiliates..

C. The Effect of the PTAR on Syndicated Program Quality

A primary motivation for the adoption of the PTAR was the FCC's concern over the "virtual disappearance of high cost, prime time, syndicated programming, the type of programming . . . that must be most relied upon as competition for network-supplied entertainment programs."[47] By compelling network affiliates to allocate a portion of prime time to nonnetwork programming, the FCC intended to reverse this trend. The FCC also hoped that greater program variety would be forthcoming.[48] Others, however, predicted that rule would not greatly affect the type of programming (in terms of format) offered in the

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[46] There is also empirical evidence that "clearance" rates for network-supplied programming have fallen somewhat (from about 95 percent in the 1970s to about 90 percent now). See Lin, "Changing Network-Affiliate Relations Amidst a Competitive Video Marketplace," Journal of Media Economics 7 (1994), 1-12, p. 3.

[47] 23 F.C.C. 2d (1970) 385.

[48] 23 F.C.C. 2d (1970) 395.

access slot,[49] although the quality (measured in terms of production expenditures) would likely fall somewhat owing to foregone distributional efficiencies.[50] These observers also predicted that the economies associated with distributing the same program across numerous geographic markets would lead to the same degree of programming homogeneity that the rule was intended to mitigate.[51]

Critics of PTAR predicted a reduction in access period programming expenditures for the following reason. The amount spent on a program will be determined, to a great extent, by the size of its likely audience. Expected audience size for a network program, in turn, will be affected greatly by the number of affiliates clearing the program. PTAR prevents using the most efficient mechanism — an established network — for achieving widespread clearance. From a network affiliate's perspective, the next best alternative was first-run syndicated programming. Although a syndicated program typically is sold to affiliates in different

[49] An inspection of prime time programming in the three years preceding adoption of PTAR shows that the 7:00 to 7:30 time slot was not programmed by the networks (except for Sunday). The Monday through Friday 7:30 to 8:00 p.m. slot was programmed with a mixture of dramas (e.g., Gunsmoke), situation comedies (e.g., The Brady Bunch), and variety shows (e.g., The Flip Wilson Show). See Brooks and Marsh, The Complete Directory of Prime Time Network Television, 1946 to Present (5th ed.), 1992.

[50] See, e.g., Crandall, supra note 28, p. 406; Besen et al., supra note 29, p. 142; Owen and Wildman, supra note 25, p. 179; Special Staff Report, supra note 31, p. 737.

[51] Crandall, for example (supra note 28, p. 406), observed that "[p]roduction costs dominate the total costs of distributing television programs on networks or off, and the economies of large scale available from simply distributing the same film or tape across several hundred markets will inevitably lead to the same type of market 'control' so decried by the Commission."